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Supreme Court of the United States

OCTOBER TERM, 1942.

No. 476

AMERICAN INSURANCE COMPANY ET AL.,
PETITIONERS,

VS.

EDWARD L. SCHEUFLER (SUCCESSOR), SUPERINTENDENT OF THE INSURANCE DEPARTMENT OF THE STATE OF MISSOURI, ET AL.,
RESPONDENTS.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

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INDEX

Summary Statement of the Matter Involved 3

Jurisdiction 8

The Date of the Judgment to Be Reviewed 8

Questions Presented 8

Reasons Relied Upon for the Allowance of the Writ—

I. The C. C. A. held that the $8,000,000 "impounded" rate funds should be paid to the policyholders, without any decision (1) as to who owned the funds, or (2) whether or not the prior rates were confiscatory, and the increased rates lawful.

That holding is in conflict with U. S. vs. Morgan, 307 U. S. 183, 193, 197 10

II. The C. C. A. held that the petitioners were not entitled to have the rate controversy decided upon its merits [and the ownership of the $8,000,000 impounded funds thereby determined], on the ground that the petitioners had "unclean hands" which deprived them of any right to ask a court of equity to grant them the equitable relief prayed for in their suits; the misconduct consisting—not of any personal guilt, or of any knowledge, by the companies, or by any of their officers, but solely by charging them with IMPLIED knowledge of the misconduct of an alleged (but disputed) agent, Mr. Street.

The C. C. A. is in conflict with the Circuit Courts of Appeals of the Second and Seventh Circuits in Art Metal Works vs. Abraham & Straus, 107 F. 2d 944, and Hedman Mfg. Co. vs. Todd Protectograph Co., 265 Fed. 273, as well as in conflict with the general Federal and State court rule as stated in Associated Press vs. International News Service, 240 Fed. 983, 989 [affirmed on other grounds in 245 Fed. 244, 248 U. S. 215], and Vulcan Detinning Co. vs. American Can Co., 72 N. J. Eq. 387 14-15

III. The C. C. A. held that the Insurance Companies had unclean hands because of misconduct of Street which had no relationship to the equity of the Insurance Companies involved in the merits of their original suits—which holding is in conflict with the decision of this court in Keystone Driller Co. vs. General Excavator Co., 290 U. S. 240, 245, with the decisions of other Circuit Courts of Appeals on the same matter in Primeau vs. Granfield, 193 Fed. 911, 916 (C. C. A. 2nd); Goodyear Tire & Rubber Co. vs. Overman Cushion Tire Co., 95 F. 2d 978, 982 (C. C. A. 6th); Knapp vs. S. Jarvis Adams Co., 135 Fed. 1008, 1010 (C. C. A. 6th); Bentley vs. Tibbals, 223 Fed. 247, 252 (C. C. A. 2nd), and with the decisions of the Supreme Court of Missouri in Krug vs. Bremer, 316 Mo. 891, 292 S. W. 702, and Stegman vs. Weeke, 279 Mo. 131, 214 S. W. 134 19

TABLE OF CASES

American Insurance Co. vs. Scheufler et al., 129 F. 2d 143 1
Art Metal Works vs. Abraham & Straus, 107 F. 2d 944 ..... 15, 17
Associated Press vs. International News Service, 240 Fed. 983, 989 (affirmed 245 Fed. 244, 248 U. S. 215) 15, 17
Bentley vs. Tibbals, 223 Fed. 247, 252 (C. C. A. 2nd) 19, 21
Bronson vs. Schulten, 104 U. S. 410, 415 14
Chute vs. Wisconsin Chemical Co., 185 Fed. 115, 118 22
Delaware, L. & W. R. Co. vs. Rellstab, 276 U. S. 1 13
Goodyear Tire & Rubber Co. vs. Overman Cushion Tire Co., 95 F. 2d 978, 982 (C. C. A. 6th) 19
Hedman Mfg. Co. vs. Todd Protectograph Co., 265 Fed. 273, 278 ..... 15, 16, 18
In re Metropolitan Trust Company, 218 U. S. 312, 320 13
Keystone Driller Co. vs. General Excavator Co., 290 U. S. 240, 245 ..... 19, 20
Knapp vs. S. Jarvis Adams Co., 135 Fed. 1008, 1010 (C. C. A. 6th) 19

Krug vs. Bremer, 316 Mo. 891, 892, 899, 292 S. W. 702, 705 ..... 19, 21
Mason vs. Kansas City Belt Railway Co., 226 Mo. 212, 223, 224, 125 S. W. 1128, 1132 13
Miocene Ditch Co. vs. Campion Mining & Trading Co., 197 Fed. 497 13
Nelson vs. Meeham, 155 Fed. 1, 6 13
O'Connor vs. O'Connor et al., 142 Fed. 449, 450 13
Phillips vs. Negley, 117 U. S. 665 14
Primeau vs. Granfield, 193 Fed. 911, 916 (C. C. A. 2nd) 19, 20
Stegmann vs. Weeke, 279 Mo. 131, 214 S. W. 134 ..... 19, 22
U. S. vs. Pendergast, 28 F. Supp. 601 4
U. S. vs. Morgan, 307 U. S. 183, 193, 197 10
Vulcan Detinning Co. vs. American Can Co., 72 N. J. Eq. 387 15

STATUTES

Act of February 13, 1925, C. 229, Section 8, 43 Stat. 940 (Title 28, U. S. C. A., Section 350) 8
Judicial Code, Section 240, as amended by Act of February 13, 1925, C. 229, Section 1, 43 Stat. 938 (Title 28, U. S. C. A., Section 347) 8

TEXTBOOK

2 Pomeroy's Eq. Jur. (5th Ed.), Sec. 592 18

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RESPONDENTS.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

To the Honorable the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Your Petitioners American Insurance Company and other Fire Insurance companies whose names are signed to this petition, severally petition for a writ of *certiorari* to the Circuit Court of Appeals (8th Circuit) to review its decision in *American Insurance Co.* v. *Scheufler et al.*, 129 F. 2d 143 (R. Vol. V, p. 16), distributing to policyholders over $8,000,000 "impounded" funds (*i. e.* increases in fire insurance rates impounded under interlocutory injunctions)—all (1) without the C. C. A. ever deciding

who owned the $8,000,000 fund, and (2) with the C. C. A. *refusing to decide* whether the increases in rates were lawful or not.

The facts are absolutely undisputed.

This Court has just granted certiorari to review the judgment of the *same* three-judge court (Stone, Otis, Reeves, J. J.) and the *same* C. C. A. (Eighth), which imposed two-year sentences (for contempt of court) upon Pendergast, O'Malley and McCormack. Those three men, in conjunction with one Street (deceased vice-president of five fire insurance companies) perpetrated an outrageous fraud upon the three-judge court; and also perpetrated the same fraud (i) upon all of the attorneys on both sides, to-wit for O'Malley and for the petitioners, and (ii) upon all the present petitioners themselves.

By two-year sentences, the lower courts punished these three living guilty perpetrators of the fraud.

By denying the petitioners here any decision as to their ownership of about eight million dollars "impounded" funds, the *same* lower courts thus punished the petitioners who were wholly innocent and absolutely ignorant* of any facts concerning the fraud.

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*The undisputed evidence (consisting of nearly 100 witnesses testifying in the three-judge court's own elaborate investigation through a Special Master) and the investigations of several grand juries, *First*, established without contradiction that Pendergast, O'Malley, McCormack and Street were the sole perpetrators of the fraud, and, *Second*, established without contradiction that no officer, agent, or employe of any of 134 petitioners knew of or had any connection with (i) any act of Pendergast, O'Malley or McCormack concerning the payment or the receipt of any money directly or indirectly connected with Pendergast, O'Malley or McCormack, or connected in any way with the fraud perpetrated upon the Court, or (ii) with any act of Street concerning the payment of any moneys directly or indirectly connected with the fraud, or for any other purpose, except that the New York and Hartford Companies (54 Companies) advanced to Street $100,000 for the payment of lawyers' fees which Street represented to them he would have to employ because the other lawyers previously employed were *persona non grata* to the Missouri authorities. As to 5 petitioners, Great American Insurance Company, American Alliance Insurance Company, County Fire Insurance Company of Philadelphia, Detroit Fire & Marine Insurance Company, and Massachusetts Fire & Marine Insurance Company, they were equally ignorant except so far as Street's knowledge as an executive officer might be the knowledge of the 5 companies.

As this Court has just granted certiorari to review the action of the lower courts in punishing the three living guilty perpetrators of the fraud, it should also grant certiorari to review the judgments of the same lower courts punishing the innocent petitioners by denying them the right to a decision as to the ownership of the eight million dollars.

The evidence in both sets of cases is the same, except that, in the cases at bar, nearly 100 witnesses affirmatively proved, without contradiction, that none of the 229 officers of the petitioners knew Pendergast, or O'Malley, and that they had absolutely no knowledge of the fraud or of any of the facts connected therewith, perpetrated by Pendergast, O'Malley and Street.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

In May, 1930, the petitioners filed separate suits (consolidated for purpose of appeal, R. Vol. A, p. 16, Vol. V, p. 1) to enjoin the Superintendent of Insurance and Attorney General of Missouri from interfering with the petitioners' collection of a 16 2/3% increase in rates, on the ground that the prior rates were confiscatory; that the 16 2/3% increase was reasonable; and that the threatened acts of the Superintendent of Insurance and Attorney General, and the Missouri Statutes under which they claimed to act, were confiscatory, and unconstitutional under the 14th Amendment.

On July 2, 1930, the 3-Judge Court enjoined any interference with the collection of the 16 2/3% increase, but upon condition that the 16 2/3% increased rates, when collected, should be impounded and paid to the Court's Custodian (R. 19-25, Vol. A); and about $10,000,000 was so "impounded" in the Court's custody.

A Special Master was appointed, and after hearing a great deal of testimony filed separate reports with Find-

ings of Fact and Conclusions of Law in each of the 137 cases which were uniformly favorable to petitioners (R. Vol. A, p. 205, *U. S.* v. *Pendergast*, 28 F. Supp. 601).

On May 18, 1935, C. R. Street, who was Vice President of 5 companies, and Chairman of a small committee which in a supervisory and advisory capacity had charge of the Missouri Rate Litigation, entered into an agreement of settlement under which the Superintendent was to make and file a Rate Order approving, retroactively to June 1st, 1930, 80% of the increase, and disapproving the remaining 20%. Street had specific authority from 54 of the petitioners to make the settlement, but the remaining 85 petitioners gave him no authority, and had no prior knowledge of the settlement. He assumed to act for them.

On February 1, 1936, the District Court upon motion for decrees based upon this Rate Order, and upon a Stipulation of the parties entered a Consent Decree in each case, by which it was ordered that 80% of the monies which had been impounded pursuant to the Interlocutory Injunctions should be paid to petitioners, and 20% to the policyholders, and that each case be dismissed (R. Vol. A, p. 212).

Early in 1939, as the result of the accidental discovery of certain facts, and after an exhaustive investigation conducted by the Bureau of Internal Revenue, and by the Justice Department, it was discovered that C. R. Street had paid $440,000 to one T. J. Pendergast, a Missouri political boss, to bring about a settlement of the Missouri rate litigation, and that Pendergast had paid to the Superintendent of Insurance a substantial sum out of this $440,000. Street had obtained $100,000 of this $440,000 from 54 of the petitioners and their authority to settle the litigation upon representations made to their Executive Officers that conditions in the fire insurance business in Missouri were chaotic, the rate litigation should be settled, that the attorneys representing the petitioners had become *persona non grata* in the State of Missouri, and that he would have to employ new lawyers. He promised a

complete accounting when the whole matter was closed.

Under the final decrees 30% out of the 80% going to petitioners was paid to Street and R. J. Folonie, as Trustees, to take care of certain expenses. In March, 1936, Street and Folonie distributed 11% out of this 30% to petitioners. At the time this distribution was made, Street, without knowledge of Folonie, and upon the misrepresentation that he had incurred additional legal expense, asked petitioners to pay back 5% out of this 11%.* Without question, and as a routine matter, every one of the Insurance Companies so requested, gave checks to Street for this 5%, thus providing him with approximately $340,000 which he paid to Pendergast. On October 28th, effective November 11, 1935, complete new rate schedules were filed and approved by the Superintendent, thus doing away with the necessity for further impounding.

No representative of any of the petitioners had any knowledge of Street's promises to pay Pendergast, or of the payments made by him to Pendergast, and Street himself did not know that any of the money which he had promised to pay Pendergast, or which he paid to Pendergast, was to go to the Superintendent of Insurance.

When petitioners first learned of the misconduct of Street, and about April 8, 1939, they decided to present in the District Court the whole situation regarding the February 1, 1936, Consent Decree, but upon being advised that any action they might take might hamper the United States, they delayed action until after Pendergast and O'Malley pleaded guilty (Vol. A, pp. 238, 239, 242, 244).

On May 29, 1939, the Superintendent of Insurance without prior notice to petitioners filed in each of the 137 cases a motion that the petitioners be cited to show cause why the decrees of February 1, 1936, should not be set aside to the extent of the distribution made thereunder, and that the petitioners, and each of them, be ordered to

*The 54 companies who had advanced the $100,000 were advised to deduct from this 5% their previous advancements.

pay to the custodian the full 80% of the impounded funds distributed to them, together with interest.

On the same day, May 29, 1939, the three-Judge District Court, without hearing any evidence, entered in each of the 137 cases two orders. One was upon the motion for citation with the consent of petitioners, and by it the petitioners were ordered, on or before July 1, 1939, to pay to the custodian all amounts paid and distributed to them, and to Charles R. Street and R. J. Folonie, Trustees. The other order, which was entered on the court's own motion (the motion for citation did not pray for it, and the Superintendent's counsel disclaimed that as one of its purposes) (Vol. A, p. 240), ordered Petitioners to show cause why the impounded premiums should not be restored to the policyholders "and this cause dismissed" (R. Vol. A, p. 251).

Each of the petitioners filed its return to this show-cause order on June 15, 1939. In these returns, after denying that C. R. Street, or any other person, was authorized to commit bribery or to pay any moneys to induce official action, or to consent to so doing, and after denying knowledge of or participation in any supposed bribery, or payment of moneys to induce official action, and after a disaffirmance of any advantage in any wise arising from the decree of February 1, 1936, either upon the settlement or rate order forming the basis thereof, they alleged that the Court could "make distribution of the sums in its possession only according to law to the lawful owners of said monies as may be determined upon an appropriate hearing and determination of the merits of the controversy as set forth in the pleadings of the respective parties and pursuant to the evidence and Master's Report and exceptions thereto"; and prayed that the Superintendent show cause "why the Court should not proceed with the determination of the merits of the controversy between plaintiffs and defendant as in their pleadings set forth" (R. Vol. A, pp. 257, 258).

On July 3, 1939, the District Court appointed a Special Master, before whom the facts above set forth relating to the misconduct of Street, and the lack of knowledge thereof by petitioners, were developed. Some 97 witnesses testified before the Special Master, most of whom were Officers and Executives of petitioners. They were men of the highest standing in the business world. Their reactions in the whole matter were the same, and the Master was satisfied with their credibility (R. Vol. IV, p. 5).

The 3-Judge District Court did not find that any of the petitioners had any knowledge of the misconduct of Street in connection with the settlement, except the five petitioners, of which Street was Vice President and Western Manager,* but that Court found that, with the exception of the five petitioners noted above, petitioners had implied knowledge of Street's misconduct, *i. e.*, they had knowledge of facts which the Court asserted would put a reasonably prudent person upon inquiry, and had reasonably diligent inquiry been made by them they would have discovered that Street was using improper means to obtain a settlement in time to have prevented a fraud upon the Court (Finding of Fact 9, R. Vol. A, p. 409, and Conclusions of Law, B and D, R. Vol. A, p. 410).

The District Court held that because of this alleged implied knowledge the petitioners were in court with unclean hands, and *were not entitled* to have the cases tried on the merits (R. Vol. A, pp. 410, 411, 398 *et seq.*). By its decree entered August 14, 1940, it set aside the 1936 decree entered in each of said 137 cases insofar as said decree directed payment of 80% of the impounded funds to petitioners, and ordered the custodian to pay to the policyholders the funds then in his custody, with interest (Vol. A, p. 412).

The Court of Appeals affirmed this decree.

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*Great American Insurance Company, American Alliance Insurance Company, County Fire Insurance Company of Philadelphia, Detroit Fire & Marine Insurance Company, and Massachusetts Fire & Marine Insurance Company.

JURISDICTION.

The jurisdiction of this Court is invoked by petitioners for writs of certiorari under Section 240 of the Judicial Code, as amended by Act of February 13, 1925, C. 229, Section 1, 43 Stat. 938 (Title 28, U. S. C. A., Section 347), and under the same Act, C. 229, Section 8, 43 Stat. 940 (Title 28, U. S. C. A., Section 350).

THE DATE OF THE JUDGMENT TO BE REVIEWED.

The judgment of the Circuit Court of Appeals affirming the decree of the District Court was entered on the 25th day of July, 1942 (R. Vol. V, p. 26).

QUESTIONS PRESENTED.

I.

Can the 3-Judge Court (1) refuse to determine the merits of the rate controversy, and (2) distribute the funds impounded under the interlocutory injunctions without determination of their ownership?

II.

Did the show cause orders (entered in each petitioner's case) automatically set aside the decrees of February 1, 1936, dismissing the cause, and thereby leave the 3-Judge Court absolutely free to determine the merits of the petitioners' original suits, to-wit, whether the impounded funds should be paid to the policyholders or should be paid to petitioners?

III.

Were petitioners deprived of the right to a decision of their original suits on the merits, by the application to them

of the equitable maxim that "He who comes into equity must come with clean hands," on the ground that the settlement and dismissal of their suits had been procured by the fraud of C. R. Street, which fraud petitioners did not authorize, and of which they had no personal knowledge, and which they repudiated promptly upon the discovery thereof?

IV.

Can the "unclean hands" doctrine be invoked against petitioners upon the basis that they had *implied* knowledge of the misconduct of C. R. Street—the petitioners *not having any personal knowledge* of such misconduct?

V.

Did the misconduct of C. R. Street in fraudulently bringing about a settlement of petitioners' suits, after they were tried and submitted (which fraud petitioners repudiated upon discovery thereof), have an immediate and necessary relationship to the equity which petitioners sought, that is, an adjudication of the ownership of the impounded premiums by a determination of the merits of their original suits, so as to justify the application to them of the "unclean hands" doctrine?

REASONS RELIED UPON FOR THE ALLOWANCE OF THE WRIT.

I.

The C. C. A. held that the $8,000,000 "impounded" rate funds should be paid to the policyholders, without any decision (1) as to who owned the funds, or (2) whether or not the prior rates were confiscatory, and the increased rates lawful.

That holding is in conflict with U. S. v. Morgan, 307 U. S. 183, 193, 197.

1. The 3-Judge Court and the C. C. A. (1) ordered the $8,000,000 distributed to the policyholders and (2) refused to decide (*a*) the merits of the rate controversy; or (*b*) who owned the impounded funds; or (*c*) whether the prior rates were confiscatory; or (*d*) whether the increased rates from which the impunded funds arose were reasonable.

Certiorari should be granted, because that holding is in conflict with *U. S.* v. *Morgan*, 307 U. S. 183. In that case a 3-Judge Court (two members being on the 3-Judge Court in the case at bar) impounded a rate fund, arising from the difference between rates collected, and reduced rates ordered.

This court held that such an "impounded" rate fund could not be *ipso facto* distributed to either party, but must abide an ultimate decision as to whether the old, or the reduced, rates were the lawful ones to be charged, saying (307 U. S., at pp. 193, 197):

> "Its action presupposed that the ownership of the excess payments was in doubt and could be finally determined only by an adjudiciation on the merits of the reasonableness of the filed rates. In taking the payments into custody it acted as a court of equity, charged both with the responsibility of protecting the

fund and of disposing of it according to law, and free in the discharge of that duty to use broad discretion in the exercise of its powers in such manner as to avoid an unjust or unlawful result. * * *

While at the moment appellants are content with inaction, and it is appellees who are demanding action—the payment to them of rates whose lawfulness is challenged and not yet determined—the actual posture of the case is **such that the court is under a self-imposed duty to act by virtue of having taken the fund into its possession, and in acting to dispose of the fund it must conform to controlling legal principles"** (Emphasis supplied).

The C. C. A. ignored (without citing it) the rule in the Morgan case.

2. The C. C. A. apparently justified its action upon two theories, the judicial adoption of either of which is a sufficient reason for granting *certiorari,* to-wit:

First: The C. C. A. held that, as the February 1, 1936, Consent Decree ordered "this cause is hereby dismissed" no controversy, or bill in equity, was thereafter before the 3-Judge Court under which it could be asked to decide whether the increased rates were lawful or not; and hence that the insurance companies had no right to ask, and the 3-Judge Court had no right to decide, anything regarding the ownership of the $8,000,000 impounded funds.

On May 29, 1939, the 3-Judge Court, without evidence, but upon the Pendergast and O'Malley "Pleas of Guilty," ordered the Insurance Companies to restore to the Court's custody over $7,000,000, which the Court had distributed to the companies under the February 1, 1936, Consent Decree.

By so doing, the 3-Judge Court *asserted its power* to summarily set aside a Final Decree *more than three years old.* That judicial action automatically set aside the old February 1, 1936, decree, including that part which ordered "this cause is hereby dismissed." Therefore, after May 29,

1939, the February 1, 1936, Consent Decree had been set aside *in toto;* and the 137 Bills in Equity were automatically reinstated, so that the 3-Judge Court had full jurisdiction to decide the causes upon the merits.

On May 29, 1939, the 3-Judge Court recognized that its order of that day (compelling the petitioners to restore to the Court so much of the impounded fund as had been distributed to them under the February 1, 1936, Decree), *automatically set aside* the entire Decree of February 1, 1936, dismissing the causes.

This is so, because:

First: The 3-Judge Court ordered the Companies (in each separate suit) to show cause why this cause should not be dismissed, which would have been senseless unless the February 1, 1936, dismissals *had already been set aside* and the causes reinstated. The petitioners, in their returns to the order to show cause, alleged that to dismiss their causes without an adjudication of the reasonableness of the increased rates, and of the ownership of the impounded funds (upon the merits of their suits) would be "unlawful and inequitable" (R. Vol. A, p. 256) thus accepting the show cause order as meaning what it said.

Second: If the C. C. A.'s theory is correct, [*i. e.*, that the 137 suits had been dismissed and never reinstated, and consequently there was nothing before the Court to decide], then it was senseless for the 3-Judge Court to have appointed a Special Master and have taken 1,600 pages of testimony upon the 3-Judge Court's power to dispose of the impounded funds.

That is a singular contradiction between the 3-Judge Court's theory (towit that they had to take an immense amount of testimony in order to decide what they would do with the impounded funds) and the C. C. A.'s theory (towit, that the 3-Judge Court could not under any circumstances decide anything about the title to impounded funds); and could only return them to the Policyholders,

without any consideration of the merits, or of the circumstances surrounding the entry of the February 1, 1936, Decree.

Moreover under the law, if the dismissals were not automatically vacated by these orders, then every order which the Court made after May 29, 1939, including the show-cause order was absolutely void because it is academic that if there is no case pending a Court has no power to make an order *in it* as distinguished from an order on the decree to effectuate the decree. *Mason* v. *Kansas City Belt Railway Co.*, 226 Mo. 212, 223, 224, 125 S. W. 1128, 1132.

The C. C. A.'s action justifies certiorari in order to prevent the doctrine stated by it from becoming an authoritative statement of the law regarding the power of Federal Courts to modify or set aside ancient decrees or judgments. This is so because:

Third. If the C. C. A. is correct, then (upon application, upon the basis of newspaper publications, or after some supposed result in other litigations), every Federal Court may, at will, set aside any part of any ancient decree it chooses to vacate; and yet, at the same time, leave all the rest of such decree (as the C. C. A. here holds) in full force and effect.*

No such doctrine has ever heretofore been adopted by any Court.

After the expiration of the term at which a Decree is entered, the Court has no jurisdiction to modify it, or to set it aside, except through an independent suit in equity based on certain specified grounds. *In re Metropolitan Trust Company*, 218 U. S. 312, 320; *Delaware, L. & W. R. Co.* v. *Rellstab*, 276 U. S. 1; *O'Connor* v. *O'Connor et al.*, 142 Fed. 449, 450; *Nelson* v. *Meeham*, 155 Fed. 1, 6; *Miocene Ditch Co.* v. *Campion Mining & Trading Co.*, 197 Fed. 497;

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*The term at which these decrees were entered expired April 26, 1936.

Bronson v. *Schulten*, 104 U. S. 410, 415; *Phillips* v. *Negley*, 117 U. S. 665.

In the interest of the orderly administration of judicial proceedings, this Court should determine (1) whether years after a final Decree has been entered, any Court, by its *ipse dixit*, may, without evidence, vacate certain parts of a Decree, disturb the rights of the parties obtained thereunder, and yet leave *other parts* of the same Decree in full force and effect; and (2) whether the Court may simultaneously assert that, because it did not choose to set aside other parts of the same old Decree, the Court is without power to deal with the cause, except as to those parts of the old Decree which it elected to set aside.

Such a doctrine would (*a*) leave every litigant in perpetual helplessness as against a Court's long subsequent determination to vacate an ancient Decree, and (*b*) destroy the established law that a Decree can not be modified after the term except (i) by appeal, or (ii) by independent suit in equity based on certain specified grounds.

II.

The C. C. A. held* that the petitioners were not entitled to have the rate controversy decided upon its merits [and the ownership of the $8,000,000 impounded funds thereby determined], on the ground that the petitioners had "unclean hands" which deprived them of any right to ask a court of equity to grant them the equitable relief prayed for in their suits; the misconduct consisting—not of any personal guilt, or of any knowledge, by the companies, or by any of their officers, but solely by charging them with IMPLIED knowledge of the misconduct of an alleged (but disputed) agent, Mr. Street.

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*Even *assuming* (1) that the Decrees of February 1, 1936 (dismissing the causes), had been *set aside* completely; and (2) that the Bills in Equity with all the Testimony and the Master's Report, *were in full force and effect*—and all pending before the 3-Judge Court, awaiting a decision by it upon the merits.

The C. C. A. is in conflict with the Circuit Courts of Appeals of the Second and Seventh Circuits in Art Metal Works v. Abraham & Straus, 107 F. 2d 944, and Hedman Mfg. Co. v. Todd Protectograph Co., 265 Fed. 273, as well as in conflict with the general Federal and State court rule as stated in Associated Press v. International News Service, 240 Fed. 983, 989 [affirmed on other grounds in 245 Fed. 244, 248 U. S. 215], and Vulcan Detinning Co. v. American Can Co., 72 N. J. Eq. 387.

The C. C. A. said that the petitioners were not entitled to have the rate controversy decided upon its merits, and the ownership of the impounded funds thereby determined, on the ground that

> "they [Insurance Companies] had been guilty of misconduct with reference to these very suits, and a litigant coming into a court of equity must keep his hands clean throughout the litigation" (R. Vol. V, p. 25).

The conflict between the C. C. A. here, and the Second and Seventh Circuits lies in, and is unconsciously concealed by, the ambiguous nature of the term "misconduct."

The 3-Judge Court's searching investigations—through the District Attorney's office, two grand juries, and the testimony of 97 witnesses (covering 1,600 printed pages, and 678 pages of a Special Master's report thereon) established without contradiction that (except for Mr. Street himself) no officer, agent, employee or attorney of any of the 139 Insurance Companies, had any knowledge of Street's misconduct, or use of money, or other wrongful acts, in connection with Pendergast, Superintendent O'Malley, or anyone else.

Nevertheless, the 3-Judge Court and the C. C. A. held the Insurance Companies guilty of "unclean hands" on the ground that they had "implied knowledge" of Street's misconduct; and that the doctrine of "unclean

hands" should be applied to a litigant, not on the basis of his actual participation in, or knowledge of, an agent's misconduct, but because he is supposed to have "implied knowledge" of such "misconduct."

That holding is in direct conflict with the Second and Seventh Circuit Courts of Appeals, and therefore Certiorari should be granted.

In the case of *Hedman Mfg. Co.* v. *Todd Protectograph Co.*, 265 Fed. 273, 278, the Circuit Court of Appeals of the 7th Circuit said:

> "This raises the question whether unfair business practices on the part of an agent, unknown to and unauthorized by his principal, and for which the principal might be liable in damages and to injunctive relief against continuance of the conduct, would, on the 'unclean hands' doctrine, prevent the principal from obtaining equitable relief against the person thus injured by the acts of the agents for unfair trade practices of such person toward the principal. The authorities upon this question are not numerous. A case quite in point is that of *Vulcan Detinning Co.* v. *American Can Co.*, 72 N. J. Eq. 387, 67 Atl. 339, 12 L. R. A. (N. S.) 102, wherein it was said:
>
> > 'That the knowledge possessed by an agent, but not acquired by him while acting for his principal, will under certain conditions be imputed to the latter, is in the nature of a presumption indulged in by courts in working out the rights of litigating parties. * * * An essential part of the presumption in question is that the principal is ignorant of the knowledge that has been casually acquired by his agent. * * * True, he may be bound by it in the sense that his legal rights may be determined with reference to the knowledge with which he is thus chargeable; but his conscience is void of offense, and hence it cannot with any propriety be said that his hands are unclean, for "unclean hands," within the meaning of the maxim of equity, is a figurative description of a class of suitors to whom a court of equity

> as a court of conscience will not even listen, because the conduct of such suitors is itself unconscionable—*i. e.*, morally reprehensible as to known facts.'
>
> *Associated Press* v. *International News Service*, (D. C.) 240 Fed. 983, is to like effect."

In the case of *Associated Press* v. *International News Service*, 240 Fed. 983, 989 (affirmed in 245 Fed. 244, 248 U. S. 215), cited with approval in the Hedman case, the Court said:

> "Now the doctrine that he who comes into equity must come in with clean hands does not recognize mere imputations of guilt based upon technical theories of agency. To invoke it a knowledge must exist on the part of the principal of the facts upon which the charge of unconscionable conduct is based, and in the case of a corporation, those facts must be brought home to the persons exercising general control over its affairs.
>
> No such knowledge has been shown on the part of the officers or manager of the Associated Press, and the complainant consequently is not barred from seeking the relief * * *."

After the Manton scandal, the C. C. A. (2d) granted a Petition for Review of *Art Metal Works* v. *Abraham & Straus*, 70 F. 2d 641, in which Judge Manton had delivered the majority opinion reversing the Decree. The C. C. A. (2d) then affirmed the Decree on the dissenting opinion of HAND, J. [107 F. 2d 944], wherein he had said:

> "My brothers believe, since the plaintiffs were liable for their salesmen's torts, that their declarations, made within the scope of their authority, charged their employer's conscience and barred this suit. I do not; and that is really the only importance of our decision beyond the interests of the immediate parties. Whenever the question has come up, it has been held that immoral conduct, to be relevant,

must touch and taint the plaintiff personally; that the acts of his agents, though imputed to him legally, do not impugn his conscience vicariously. *Vulcan Detinning Co.* v. *American Can Co.*, 72 N. J. Eq. 387, 391, 392, 67 Atl. 339, 12 L. R. A. (N. S.) 102; *Hedman Mfg. Co.* v. *Todd Protectograph Co.*, 265 Fed. 273, 278 (C. C. A. 7); *Associated Press* v. *International News Service*, (D. C.) 240 Fed. 983, 989. Cf. *Joseph Schlitz* v. *Houston Ice & Brewing Co.*, 241 Fed. 817, 824 (C. C. A. 5). * * * It would be monstrous that a man's conscience should bear the sins of those he employs, however liable he may be for their acts, and a doctrine which stands upon moral wrongdoing must clear itself of that confusion, or adopt another form. While it stands upon the court's repugnance to the suitor personally, it must confine itself to his personal deliquencies."

The District Court recognized this rule (in fact there are no cases to the contrary), but seemed to think that there was a distinction between imputed knowledge and implied knowledge, overlooking the fact that so far as the principal here involved is concerned, both kinds of knowledge are identical. They both negative the existence of personal knowledge. The one arises out of a technical rule of agency, and the other out of a technical rule of notice. Sec. 592, 2 Pomeroy's Eq. Jur. (5th Ed.).

In neither case is the conscience of the principal tainted, and in neither case has the principal been guilty of unconscionable conduct, that is, conduct "morally reprehensible as to known facts." *Hedman Mfg. Co.* v. *Todd Protectograph Co., supra.* Not a single case is found where a principal's "implied" knowledge—there being no actual, willful, intentional, personal knowledge—has ever been made the basis of denying equitable rights to a principal on the ground of "unclean hands."

III.

The C. C. A. held that the Insurance Companies had unclean hands because of misconduct of Street which had no relationship to the equity of the Insurance Companies involved in the merits of their original suits—which holding is in conflict with the decision of this court in Keystone Driller Co. v. General Excavator Co., 290 U. S. 240, 245, with the decisions of other Circuit Courts of Appeals on the same matter in Primeau v. Granfield, 193 Fed. 911, 916 (C. C. A. 2nd); Goodyear Tire & Rubber Co. v. Overman Cushion Tire Co., 95 F. 2d 978, 982 (C. C. A. 6th); Knapp v. S. Jarvis Adams Co., 135 Fed. 1008, 1010 (C. C. A. 6th); Bentley v. Tibbals, 223 Fed. 247, 252 (C. C. A. 2nd), and with the decisions of the Supreme Court of Missouri in Krug v. Bremer, 316 Mo. 891, 292 S. W. 702, and Stegmann v. Weeke, 279 Mo. 131, 214 S. W. 134.

The equity which the Petitioners sought in these cases was to have the ownership of the funds in the possession of the Court determined by an adjudication on the merits of the original suits of the reasonableness of the 16 2/3% increase, and the confiscatory character of the prior rates. The fraud committed by C. R. Street in connection with the settlement (which settlement the Insurance Companies had repudiated upon the discovery of the fraud) had no relationship to this equity, either immediate or remote. The petitioners required no aid from Street's fraud to establish that equity. That fraud in no wise affected the equitable relations between the parties to the action. Having repudiated the fraud and restored the entire amount which had been received by or for them to the possession of the court, it cannot be said that petitioners had gained any advantage from the settlement, and the rights of the parties would necessarily have to be determined upon the issues framed by the pleadings,

the bills and answers in the original suits, without any regard to the settlement, or the fraud that procured the settlement.

In *Keystone Driller Co.* v. *General Excavator Co.*, 290 U. S. 240, 245, this Court said:

> "But courts of equity do not make the quality of suitors the test. They apply the maxim requiring clean hands only where some unconscionable act of one coming for relief *has immediate and necessary relation to the equity that he seeks in respect of the matter in litigation.* They do not close their doors because of plaintiff's misconduct, whatever its character, that has no relation to anything involved in the suit, but only for *such violations of conscience as in some measure affect the equitable relations between the parties* in respect of something brought before the Court for adjudication. Story, Eq. Jur., §100, Pomeroy, Eq. Jur., §399. They apply the maxim not by way of punishment for extraneous transgressions, but upon the considerations that make for the advancement of right and justice" (Emphasis supplied).

In *Primeau* v. *Granfield*, 193 Fed. 911, the Circuit Court of Appeals of the 2nd Circuit, page 916 of its opinion, said:

> "The wrong doing which will defeat a litigation must have connection with the matter in litigation. Misconduct in outside matters will not have such effect. A new contract upon a new consideration is not necessarily unlawful because it relates to property acquired through unlawful transactions. The real test in such a case as this is whether the plaintiff requires any aid from the fraudulent transaction to establish his demand. If he does he cannot recover. If he does not, and the cause of action is unconnected with the fraudulent undertaking and is founded upon a collateral consideration he may recover."

In *Bentley* v. *Tibbals*, 223 Fed. 247, 252, the Circuit Court of Appeals of the 2nd Circuit said:

> "We do not, however, think the maxim invoked is applicable to the case before the court. The maxim does not apply to every unconscientious act or inequitable conduct of the plaintiff. It is limited to misconduct connected with the matter in litigation, and does not apply to misconduct which is unconnected with the matter in litigation. 1 Pomeroy's Eq. Jur., §399. It is true that complainant violated the law of the United States in importing the phrase code into this country and selling it here. But, as was pointed out in *Kinner* v. *Lake Shore, etc., R. Co.*, 69 Ohio St. 339, 344, 69 N. E. 614, 615 (1903):
>
> > 'A court of equity is not an avenger of wrongs committed at large by those who resort to it for relief.'
>
> It is not sufficient to debar a suitor for relief that he has committed an unlawful act, unless that unlawful act affects the matter in litigation."

The decision of the C. C. A. is also in conflict with the decisions of the Supreme Court of Missouri.

In *Krug* v. *Bremer*, 316 Mo. 892, 899, 292 S. W. 702, 705, the situation was this: The plaintiff in the suit, an elderly widow, requested the Trustee in a mortgage to sell under foreclosure a farm which had been owned by her deceased husband so that she could buy it in and cut out the interests therein of some of her children. The suit was in equity to set aside the Trustee's sale and foreclosure upon the ground of unfairness in the sale. It was contended that her hands were unclean. The Supreme Court of Missouri said:

> "We do not think that the maxim 'unclean hands' is applicable to the facts here developed. It must relate to the particular matter involved. The

question here involved is the cancelling of the Trustee's deed, and the setting aside of the foreclosure sale for fairness on the part of the Trustee. The assertion that plaintiff's hands are unclean is enveloped in the right of protection for declining years and providing against want if possible on her part. The situations are not analogous. On the one hand she questions the Trustee's unfairness, while on the other her right to protect herself and provide against want or charity is questioned. *The question of unclean hands does not arise out of the transaction which is the subject of the suit"* (Emphasis supplied).

Quoting from *Stegmann* v. *Weeke*, 279 Mo. 131, 138, 214 S. W. 134, 136, the Court said:

"The ancient maxim that he who comes into equity must come with clean hands has been applied to various kinds of cases but it has its limitations. The particular inequity which prevents the pursuit of an equitable remedy on the part of the plaintiff must relate to the particular matter in hand, must arise out of the transaction which is the subject of the suit."

The correct principle is announced in *Chute* v. *Wisconsin Chemical Co.*, 185 Fed. 115, 118, where the Court said:

"* * * No cause of action will be proceeded with which has become infected with fraud or other inequity. It matters not when, or how, the facts are brought to the attention of the court. The distinction is, however, fundamental that the transgression which falls within this maxim must have infected the cause of action, so that to entertain it would be violative of conscience. *It does not reach a case where the cause of action is meritorious and where subsequent to suit brought the complainant has been guilty of reprehensible conduct, but which does not go to the cause of action"* (Emphasis supplied).

Wherefore, petitioners severally respectfully pray that writs of certiorari issue.

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Company, Globe and Rutgers Fire Insurance Company, Granite State Fire Insurance Company, Great American Insurance Company, Guaranty Fire Insurance Company of Providence, The Hanover Fire Insurance Company, Hartford Fire Insurance Company, The Home Insurance Company, Home Fire and Marine Insurance Company, Hudson Insurance Company, Imperial Assurance Company, Importers and Exporters Insurance Company, Insurance Company of North America, Insurance Company of the State of Pennsylvania, The Law Union and Rock Insurance Company, Ltd., Liverpool and London and Globe Insurance Company, The London Assurance Corporation, London and Lancashire Insurance Company, Ltd., London and Provincial Marine and General Ins. Co., Ltd., London and Scottish Assurance Corporation, Ltd., Lumbermen's Insurance Company, Manhattan Fire and Marine Insurance Company, Massachusetts Fire and Marine Insurance Company, Mechanics Insurance Company of Philadelphia, Merchants Insurance Company, Merchants Fire Assurance Corporation of New York, Merchants Fire Insurance Company, Mercury Insurance Company, Michigan Fire and Marine Insurance Company, Milwaukee Mechanics Insurance Company, Minneapolis Fire and Marine Insurance Company, National Ben Franklin Fire Insurance Company, National Fire Insurance Company of Hartford, National Liberty Insurance Company of America, National Reserve Insurance Company, National Security Fire Insurance Company, National Union Fire Insurance Company, The Newark Fire Insurance Company, New England Fire Insurance Company, New Hampshire Fire Insurance Company, New Jersey Insurance Company, New York Underwriters Insurance Company, Niagara Fire Insurance Company, The Northern Assurance Company, Ltd., Northern Insurance Company, North River Insurance Company, Northwestern Fire and Marine Insurance Company, Norwich Union Fire Insurance Society, Ltd., Old Colony Insurance Company, Orient Insurance Company, Pacific Fire Insurance Company, Palatine Insurance Company, Ltd., Patriotic Insurance Company of America, Philadelphia Fire and Marine Insurance Company, Phoenix Assurance Company, Ltd., The Phoenix Insurance Company, Presidential Fire and Marine Insurance Company, Providence Washington Insurance Company, Provident Fire Insurance Company, Queen Insurance Company of America, Reliance Insurance Company of Philadelphia, Rhode Island Insur-

ance Company, Royal Exchange Assurance, Royal Insurance Company, Ltd., Safeguard Insurance Company, St. Paul Fire and Marine Insurance Company, Scottish Union and National Insurance Company, Security Insurance Company of New Haven, Sentinel Fire Insurance Company, Springfield Fire and Marine Insurance Company, Standard Fire Insurance Company of Connecticut, Standard Fire Insurance Company of New Jersey, Star Insurance Company of America, The State Assurance Company, Ltd., Stuyvesant Insurance Company, Sun Insurance Office, Ltd., Superior Fire Insurance Company, Svea Fire and Life Insurance Company, Tokio Marine and Fire Insurance Company, Ltd., Transcontinental Insurance Company, The Travelers Fire Insurance Co., Twin City Fire Insurance Company, Union Assurance Society, Ltd., Union Fire Insurance Company, United Firemen's Insurance Company of Philadelphia, United States Fire Insurance Co., United States Merchants and Shippers Insurance Company, Victory Insurance Company, Westchester Fire Insurance Company, Western Assurance Company, Western Fire Insurance Company, The World Fire and Marine Insurance Company, Yorkshire Insurance Company, Ltd., Mechanics and Traders Insurance Company, Potomac Insurance Company of the District of Columbia,

Petitioners.